

Internal Revenue Service

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Person To Contact:

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Telephone Number:

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CC:PSI:B01

PLR-116926-11

Date:

September 27, 2011

Legend:

X =

State =

D1 =

D2 =

D3 =

Trust =

Y =

Z =

Dear _____ :

This responds to the letter dated March 29, 2011, and related correspondence, submitted on behalf of X, requesting relief under ' 1362(f) of the Internal Revenue Code (ACode@) for an inadvertent termination of S election.

FACTS

The information submitted states that X was organized under the laws of State on D1. X elected to be treated as an S corporation, effective D2. On D3, Trust, a grantor trust deemed to be owned by an individual (an eligible S corporation shareholder under § 1361(c)(2)(A)(i)), sold all of its stock in X to Y, an ineligible S corporation shareholder. Immediately following the sale, Y transferred the stock to eligible S corporation shareholders and Z, an ineligible S corporation shareholder.

X and its shareholders were unaware of the fact that both Y and Z were ineligible S corporation shareholders and did not intend the S election of X to terminate. After the discovery of the error, X and its shareholders took corrective actions by having Z transfer its X stock to an eligible S corporation shareholder. In addition, X and its shareholders agree to make any adjustments required by the Commissioner consistent with the treatment of X as an S corporation.

LAW AND ANALYSIS

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for the taxable year.

Section 1362(a) provides that a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

Section 1361(b)(1)(B) provides that a small business corporation cannot have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Section 1361(c)(2)(A)(i) provides that a trust, all of which is treated (under subpart E of part I of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States, may be an S corporation shareholder.

Section 1362(d)(2)(A) provides that an election under ' 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for

which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(f) provides, in part, that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consent, or (B) was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness or termination, steps were taken - (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents, and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(d) of the Income Tax Regulations provides that the Commissioner may require any adjustments that are appropriate. In general, the adjustments required should be consistent with the treatment of the corporation as an S corporation during the period specified by the Commissioner.

CONCLUSION

Based solely upon the facts submitted and the representations made, we conclude that X's S election terminated on D3. We further conclude that the termination of X's S election constituted an inadvertent termination within the meaning of § 1362(f).

Under § 1362(f), X will be treated as an S corporation from D3, and thereafter, provided that X's S election was otherwise valid and has not otherwise terminated under § 1362(d).

This ruling is contingent upon X and all its shareholders treating X as having been an S corporation for the period beginning D3, and thereafter.

Except as specifically ruled upon above, no opinion is expressed as to the federal income tax consequences of the facts described above under any other provision of the Code, including whether X was otherwise eligible to be an S corporation or whether the shareholders of X were otherwise eligible S corporation shareholders.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter ruling will be sent to your authorized representative.

Sincerely,

David R. Haglund

David R. Haglund

Chief, Branch 1

Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter

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